

## MEMORANDUM

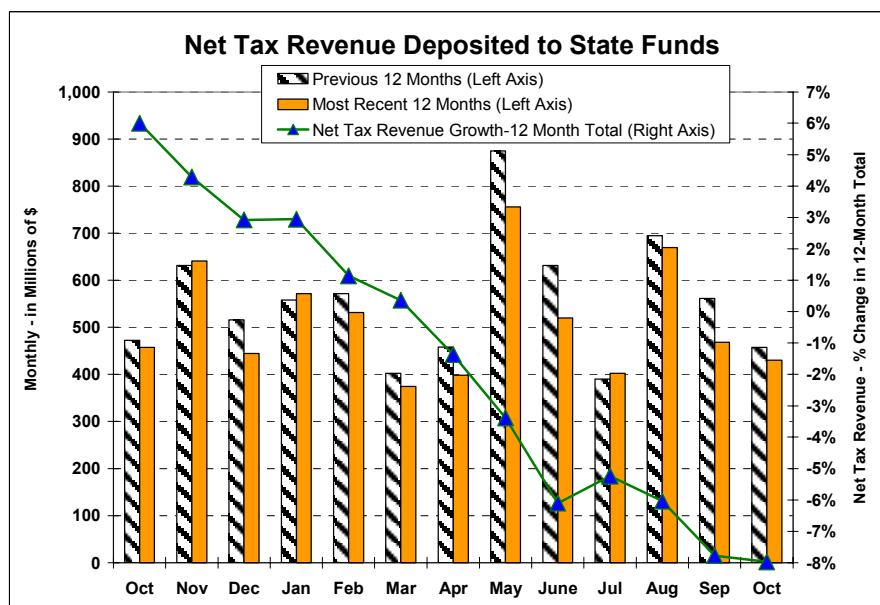
TO: Members of the Iowa Senate and  
Members of the Iowa House of Representatives

FROM: Jeff Robinson  
Shawn Snyder

DATE: November 18, 2009

### Twelve-month Total Net Tax Receipts Through October 31, 2009

The attached spreadsheet presents net State tax revenue deposited to State funds for the 12-month period ending October 2009 with comparisons to the previous 12 months. October 2008 to October 2009 one-month comparisons are also presented. The source of the information is the State accounting system, including non-General Fund accounts. All accounting transactions related to taxes remitted to the State were reviewed, along with the refunds issued against those taxes.



### Month of October Comparison

October net tax receipts totaled \$430.5 million, a decrease of \$26.8 million (- 5.9%) compared to October 2008. Major taxes and their contribution to the month's change include:

- Individual Income Tax (negative \$2.4 million, - 1.2%) – Gross income tax receipts decreased \$5.4 million in October while income tax refunds decreased \$3.0 million for the

month. Withholding payments received, a component of gross income tax receipts, increased 3.7% in October.

- Sales/Use Tax (negative \$30.8 million, - 21.4%)
  - Road Use Tax Fund use tax and fees for new registrations increased \$3.9 million, due to an accounting change that moved the destination of \$4.3 million in use tax to the Road Use Fund from the Underground Storage Tank (UST) Fund.
  - Other Fund use tax deposits decreased \$4.3 million due to a change in how the UST Fund is financed.
  - Gross General Fund sales/use tax receipts decreased \$27.4 million and refunds issued for the month increased \$3.0 million (net decrease of \$30.4 million). Approximately \$13.0 million of the decrease was due to a calendar issue that moved October deposits into November.
- Corporate Income Tax (positive \$15.8 million, 415.8%) – Net corporate tax revenue reversed course in October and posted a gain for the month. Gross receipts increased \$6.5 million and refunds decreased \$9.3 million.
- Fuel Tax (negative \$2.7 million, - 6.6%) – Gross fuel tax revenue decreased \$1.9 million while refunds processed in the month increased \$0.8 million.
- Cigarette & Tobacco Taxes (negative \$6.0 million, - 25.6%) – November receipts turned back to negative, indicating October's positive growth was likely due to deposit timing. A \$0.62 per pack federal tax increase, effective April 1, 2009, is providing downward pressure on cigarette sales.
- Gambling Tax (negative \$1.4 million, - 4.8%) – Total adjusted gross revenue for Iowa's 17 gambling facilities decreased 2.3% in October 2009, compared to October 2008, and gambling tax revenue growth has now been negative for eight consecutive months.

### **Year-over-Year Comparison – Net Tax Revenue**

During the 12-month period ending October 2009, net revenue from all taxes deposited to State funds totaled \$6.208 billion, a decrease of \$537.5 million (- 8.0%) compared to the prior 12 months. Major contributors to the year-over-year dollar and percentage changes include:

- Individual Income Tax (negative \$199.1 million, - 6.9%) – The rate of individual income tax receipt growth has decreased significantly since peaking in May 2008 at 11.8% year-over-year. The processing of tax year 2008 tax returns during the spring of 2009 accelerated the decrease. Withholding payments to the State increased \$34.3 million over the past 12 months. Of that increase, \$18.8 million was transfers of withholding from unemployment payments and \$7.1 million was transfers from State payroll, retirement, and other funds, with only \$8.4 million in growth for the year from private sector and public sector employees not part of the State accounting system. Over the previous 12 months (ending October 2008), that amount was \$134.0 million.
- Sales/Use Tax (negative \$151.5 million, - 6.7%) – Net sales/use tax receipts have been down ten of the past eleven months compared to the same month the previous year and the annual percent growth has fallen from positive 6.0% at the end of October 2008 to negative 6.7% at the end of October 2009.
- Corporate Tax (negative \$104.2 million, - 30.9%) – Net corporate income tax totaled \$232.5 million for the 12 months ending October 2009. The 12-month total peaked in June 2008 at \$371.9 million, so net corporate tax revenue is 37.5% below the latest peak. During and after the 2001 recession, net corporate tax receipts fell 68.8%, peak to trough.

- Fuel Tax (positive \$0.1 million, 0.0%) – Net motor fuel tax revenue has been weak the past twelve months, likely the result of decreased economic activity caused by the recession. According to Department of Revenue fuel sales reports, over the most recent 12-month period Iowa taxable gasoline/ethanol gallons sold increased 1.4% while taxable diesel sales were down 8.4%, the twelfth consecutive month showing a decline in annual taxable diesel sales.
- Gambling Tax (negative \$12.3 million, - 4.1%) – Despite expansions of casinos in Clinton and Dubuque, two changes providing boosts to year-over-year gambling growth, gambling tax revenue is negative year-over-year. According to Racing and Gaming Commission statistics, ten of Iowa's seventeen casino/track locations reported negative annual adjusted gross revenue (AGR) growth for the 12-month period ending October 2009. The AGR growth for all facilities was negative 2.3% over the past 12 months. Excluding the two expanded facilities, growth was negative 4.9%.
- Cigarette and Tobacco Tax (negative \$24.8 million, - 9.8%) – Iowa's indoor smoking ban and a recent increase in the federal cigarette tax are likely contributors to the tax revenue decline.
- Insurance Premium Tax (negative \$27.0 million, - 25.2%) – The decline in insurance premium tax revenue is the result of expanded use of tax credits, including credits earned through an insurance company's own activities as well as tax credits purchased from others.

### **Tax Spotlight – Individual Income Tax**

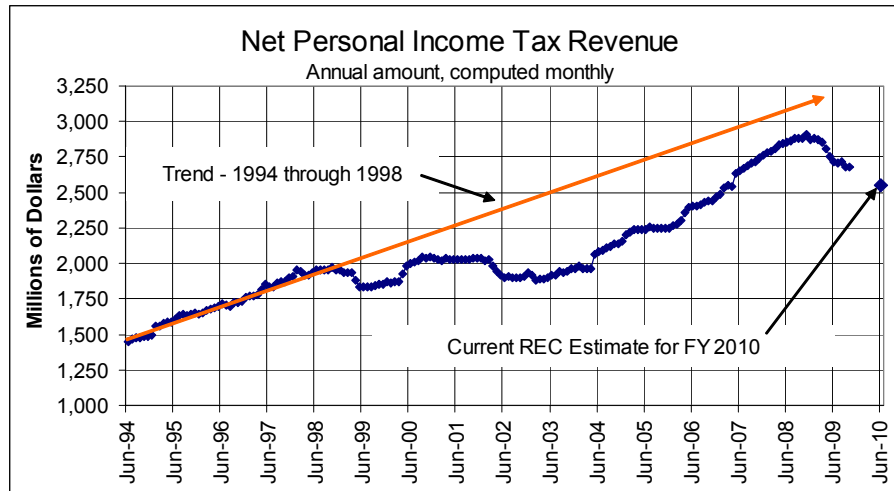
Iowa individual income is taxed under the authority of Chapter 422, Division II, Code of Iowa. The Iowa Individual Income Tax is imposed on Iowa taxable income of individuals, estates and trusts. Individuals who have a combined net income of less than \$13,500 (\$9,000 for single taxpayers) are not generally required to pay Iowa income tax or submit an Iowa income tax return. This "filing threshold" does not apply to taxpayers claimed as dependants on another tax return. Iowa uses federal adjusted gross income as the initial point for tax calculation.

The Iowa Individual Income Tax was first imposed in 1934 with a minimum marginal rate of 1.0% and a maximum marginal rate of 5.0% (HF 1 - Income, Corporation, and Sales Tax Act). The current tax rates were established in 1998 (HF 388 – Individual Income Tax Rates Act) and are applied to nine taxable income brackets ranging from a minimum marginal tax rate of 0.36% and a maximum marginal tax rate of 8.98%. The taxable income brackets are adjusted each year by the Department of Revenue based on an inflation factor. For the 2009 tax year, the maximum marginal tax rate applies to taxable income above \$63,315. Taxpayers deduct 100.0% of federal Income Tax paid when calculating taxable income. An alternative minimum tax may be imposed at an effective rate of 6.7% if it exceeds the individual, estate, or trust's regular tax liability.

There are a large number of tax credits that may provide a reduction in Individual Income Tax. A complete list is located at <http://www.state.ia.us/tax/taxlaw/Taxcredits07.pdf>. Enactment of SF 590 (Iowa Earned Income Tax Credit Act of 2007), increased the Iowa Earned Income Tax Credit from 6.5% to 7.0% of the federal credit and made the credit refundable beginning in tax year 2007.

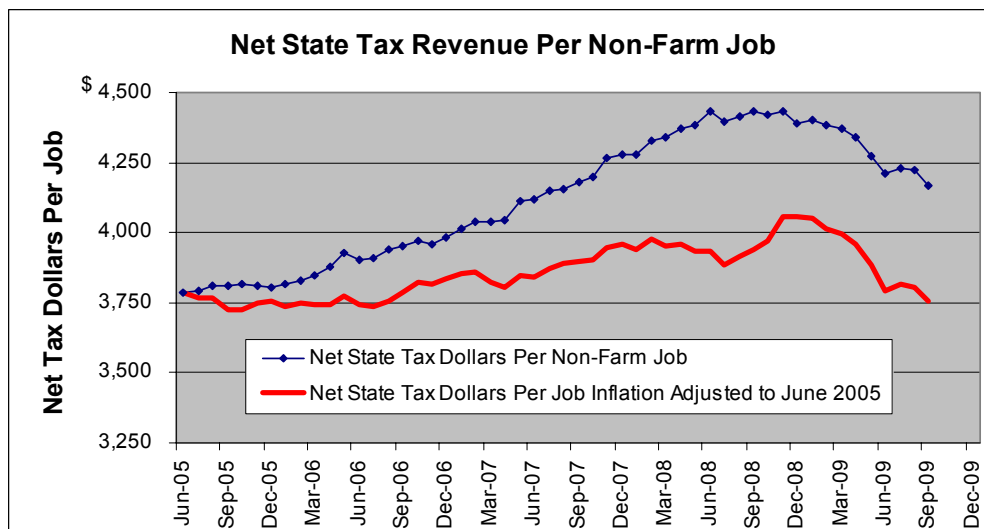
Individual income tax returns are filed by the last day of the fourth month following the end of the tax year (April 30). In some cases, individuals may be required to remit quarterly

estimated tax payments. Withholding tax is due monthly, semimonthly, or quarterly, depending on the total amount of income tax withheld. In general, Individual Income Tax revenues are deposited in the State General Fund. Pursuant to Section 422.16A, Code of Iowa, up to \$4.0 million from withholding tax is deposited in the Workforce Development Fund each year. The requirement that withholding tax receipts of \$650,000 each quarter (\$2.6 million annually) be credited to the Child Care Credit Fund was repealed in HF 811 (Department of Human Services Appropriations Act) during the 2009 Legislative Session.



## Tax Revenue and Employment

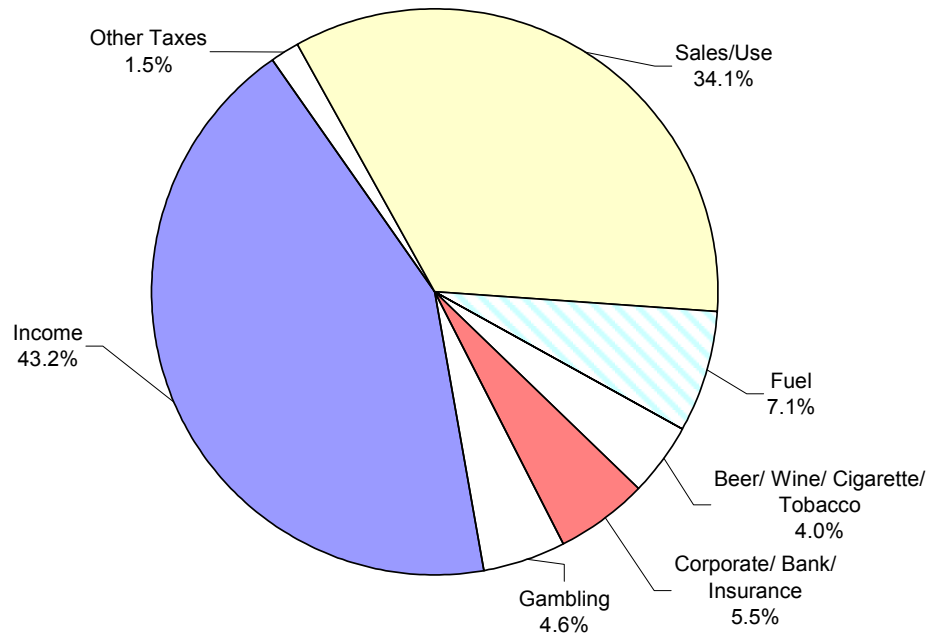
The average reading for Iowa non-farm employment over the 12 months ending September 2009 is 1,495,300, and net State tax receipts over the same 12 months totaled \$6.235 billion, or \$4,170 per non-farm job. This is \$385 (10.2%) higher than the per-job average for July 2005. Over that same time period, inflation (CPI-U) increased 11.0%. Therefore, tax revenue per job has trailed the rate of inflation since July 2005 by roughly 0.2% per year. The following chart provides an historical perspective of tax collections per non-farm job and inflation-adjusted collections per job.



## Net State Tax Revenue - Twelve Months Ending October 2009

**Net Revenue = \$6.208 Billion**

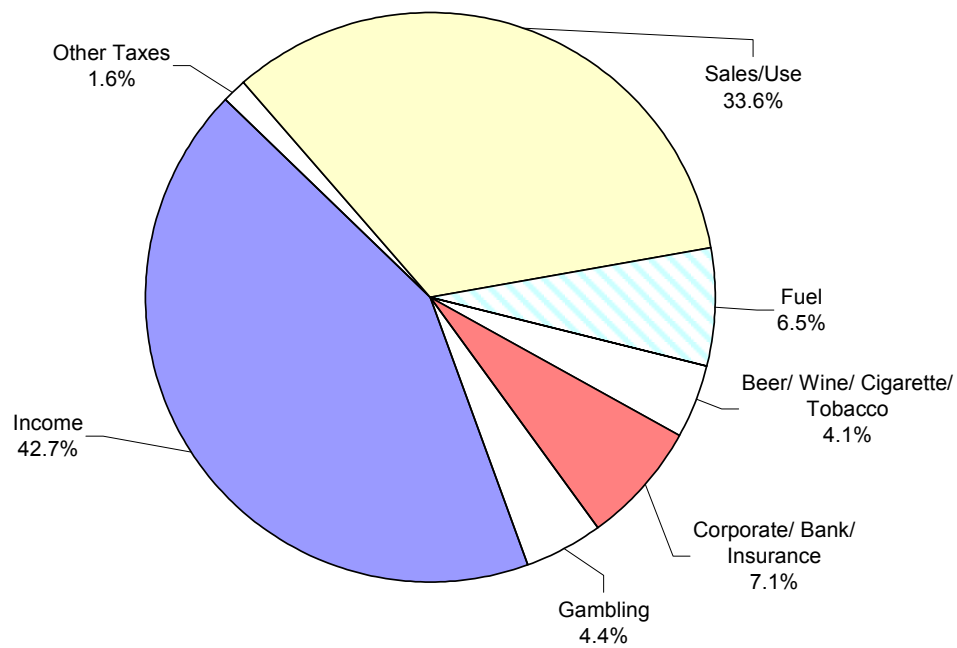
Percentages may not add to 100% due to rounding



## Net State Tax Revenue - Twelve Months Ending October 2008

**Net Revenue = \$6.746 Billion**

Percentages may not add to 100% due to rounding



## Net Tax Revenue Deposited to State Funds - Cash Basis

Dollars in millions - Columns and Rows may not add due to rounding

Net Tax by Tax Type	Previous 12-Month Period Total	Most Recent 12-Month Period Total	12-Month \$ Change	12-Month % Change	Month of October 2008	Month of October 2009	October \$ Change	October % Change
Banking	\$ 33.2	\$ 26.8	\$ - 6.4	-19.3%	\$ 3.6	\$ 1.2	\$ - 2.4	-66.7%
Beer & Wine	21.0	21.1	0.1	0.5%	1.6	1.8	0.2	12.5%
Cigarette & Tobacco	253.8	229.0	- 24.8	-9.8%	23.4	17.4	- 6.0	-25.6%
Corporate Income	336.7	232.5	- 104.2	-30.9%	3.8	19.6	15.8	415.8%
Fuel	440.9	441.0	0.1	0.0%	40.8	38.1	- 2.7	-6.6%
Gambling	299.8	287.5	- 12.3	-4.1%	29.1	27.7	- 1.4	-4.8%
Individual Income	2,879.2	2,680.1	- 199.1	-6.9%	199.3	196.9	- 2.4	-1.2%
Inheritance	84.6	70.3	- 14.3	-16.9%	8.7	10.0	1.3	14.9%
Insurance	107.3	80.3	- 27.0	-25.2%	0.0	0.0	0.0	--
Other Taxes	5.9	10.5	4.6	78.0%	1.7	3.5	1.8	105.9%
Real Estate Transfer	16.5	13.8	- 2.7	-16.4%	1.3	1.1	- 0.2	-15.4%
Sales/Use	2,266.7	2,115.2	- 151.5	-6.7%	144.0	113.2	- 30.8	-21.4%
Total Net Taxes	<u>\$ 6,745.6</u>	<u>\$ 6,208.1</u>	<u>\$ - 537.5</u>	-8.0%	<u>\$ 457.3</u>	<u>\$ 430.5</u>	<u>\$ - 26.8</u>	-5.9%
<b>Gross Tax &amp; Refunds</b>								
Gross Tax	\$ 7,583.4	\$ 7,484.3	\$ - 99.1	-1.3%	\$ 531.4	\$ 495.9	\$ - 35.5	-6.7%
Tax Refunds	\$ - 837.9	\$ - 1,276.3	\$ - 438.4	52.3%	\$ - 74.0	\$ - 65.4	\$ 8.6	-11.6%
<b>Net Tax Receipts by Fund</b>								
State General Fund (GF)	\$ 5,769.9	\$ 5,272.0	\$ - 497.9	-8.6%	\$ 360.8	\$ 346.6	\$ - 14.2	-3.9%
Road Use Tax Fund	\$ 709.7	\$ 699.3	\$ - 10.4	-1.5%	\$ 61.7	\$ 62.9	\$ 1.2	1.9%
Non-GF Gambling	\$ 237.9	\$ 219.8	\$ - 18.1	-7.6%	\$ 26.7	\$ 16.8	\$ - 9.9	-37.1%
Other State Funds	\$ 28.1	\$ 16.8	\$ - 11.3	-40.2%	\$ 8.1	\$ 4.2	\$ - 3.9	-48.1%
<b>Local Option Taxes *</b>	\$ 734.8	\$ 810.3	\$ 75.5	10.3%	\$ 49.3	\$ 54.0	\$ 4.7	9.5%

\* Sales, income, and hotel/motel. Distributed to local governments - not included in numbers above.

Numbers are rounded to the nearest \$0.1 million. Percentages are calculated after rounding.

## Tax Categories Used in Table

**Franchise (Bank) Tax:** Taxes on banks are deposited to the State General Fund. State credit union tax is included on this line also.

**Beer & Liquor Tax:** Taxes on beer, liquor, and wine are deposited to the State General Fund, the Liquor Control Fund, and a small amount is deposited to a Department of Economic Development fund for wine promotion.

**Cigarette & Tobacco Tax:** Cigarette and the tobacco products tax revenue is deposited to the State General Fund.

**Corporate Income Tax:** All corporate tax is deposited to the State General Fund.

**Motor Vehicle Fuel Tax:** All motor vehicle fuel tax is deposited to one of two road use funds, with the exception of tax revenue from the sale of aviation and marine fuels.

**Gambling Tax:** The first \$60.0 million of gambling tax revenue each fiscal year is deposited to the State General Fund (\$66.0 million beginning FY 2010). Other funds receiving deposits of gambling tax revenue over the last 24 months include the School Infrastructure Fund, the Rebuild Iowa Infrastructure Fund, The Gambler's Assistance Fund, the County Endowment Fund, and the Vision Iowa Fund.

**Individual Income Tax:** Most individual income tax revenue is deposited to the State General Fund. A total of \$4.0 million per year is deposited to the Workforce Development Fund (\$4.0 million). An annual \$2.6 million diversion to the Child Daycare Fund ended in FY 2009. In addition, several economic development programs are financed by individual income tax withholding. In those instances, the employer does not remit the tax withheld from employees and it is never deposited to a State fund. That revenue is not included here.

**Inheritance Tax:** All inheritance tax is deposited to the State General Fund.

**Insurance Premium Tax:** All insurance premium tax is deposited to the State General Fund.

**Other Taxes:** Other taxes include brucellosis eradication property tax (deposited to a Department of Agriculture and Land Stewardship fund), drug stamp tax (State General Fund), utility replacement property tax (State General Fund), and car rental tax (Road Use Tax Fund). Other taxes also include a suspense account used to hold tax deposits prior to determining the correct tax type for the money and tax revenue transferred by the Department of Revenue to separate accounts to fund tax collection activities (tax gap and Department operations).

**Real Estate Transfer Tax:** Real estate transfer tax is collected by counties. Counties retain 17.25% and remit the remainder to the State. The State deposits 95.0% to the State General Fund and 5.0% to the Shelter Assistance Fund. The distribution of real estate transfer tax revenue changes beginning FY 2010, when the State General Fund percentage begins a decline to 65.0% by FY 2015.

**Sales/Use Tax:** General sales/use tax is deposited to the State General Fund, while most vehicle use tax is deposited to the Road Use Tax Fund. Beginning FY 2009, the vehicle use tax was converted to a fee structure. To allow continuity of data, revenue from the fee structure is reflected in this document as tax revenue. Also beginning FY 2009, the School Infrastructure Local Option (SILO) sales tax was converted to a statewide 1.0% sales/use tax and the revenue from that statewide tax is transferred out of the State General Fund monthly through a refund appropriation. To allow for continuity of data, the refund transfers are subtracted as part of the net sales/use tax calculation.

**Local Option Taxes:** Local option taxes are presented at the bottom of the table and are not included in the numbers above. Prior to FY 2009, local option taxes included the SILO tax, Local Option Sales Tax (LOST) for local government finance, Local Option Income Surcharge for schools, and hotel/motel tax. Starting FY 2009, the SILO tax was converted to a 1.0% statewide tax and the SILO was eliminated. To allow for continuity of data, the transfers from the State General Fund as a result of the 1.0% statewide tax are included in the local option tax amount.

## Report Database

The database for this report is the State accounting system. If transactions are incorrectly coded in the system as tax revenue or tax refunds, the numbers presented here will be impacted.